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IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

SCANDINAVIAN-AMERICAN BANK,
a corporation,
Petitioner and Appellant.

vs.

R. L. SABIN, Trustee of the Estate
of D. Sondheim, Bankrupt,
Trustee and Respondent.

In the Matter of D. Sondheim, Bankrupt.

REPLY BRIEF OF PETITIONER AND APPELLANT

Petition for revision of and appeal from a certain order and judgment of the United States District Court for the District of Oregon.

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BOYER PRINTING COMPANY, PORTLAND, OREGON

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In his effort to support the decree of the District Court appellee, to say the least, indulges in very extravagant language and is responsible for statements concerning the position of the appellant, the facts of this case and the law applicable thereto, that are wholly unwarranted.

He charges the appellant with inconsistency. He says that the instrument, according to appellant, is "surely a chattel mortgage." The appellant has never

contended that the instrument amounted in effect to a chattel mortgage and no one knows this better than appellee, nor has the appellant amended its position from time to time after the abandonment of other equally ingenious and equally unsound contentions as appellee declares.

The appellant contended from the first, and now contends, first, that the title to the merchandise was in the bank, and therefore, that the agreement between the parties constituted a contract of conditional sale, or in any event, established such a trust relation that under the authority of In Re Cattus and like cases, it was entitled to hold the merchandise until its advances were repaid.

2. That accepting for the sake of argument, appellee's contention that the agreement amounted in effect to a chattel mortgage, it was valid under the laws of the State of Oregon and not void as contended by appellee.

3. That the appellee was without authority to maintain the proceeding. We, therefore, fail to see the occasion for appellee's charge of inconsistency.

In our brief we discussed this case under three main divisions. Adopting the same arrangement, we will answer the contentions of the appellee.

I.

Under the terms of the agreement, the title to the merchandise remained in the Bank.

Discussing this point the appellee says that under the authority of the decision of the District Court In re Rasmussen's Estate, 136 Fed. 704, and In re Roellich, 223 Fed. 687, that it is clear that in Oregon at least, such an arrangement is void as to creditors whether it is called a conditional sale, mortgage, contract, trust or by whatever nomenclature the ingenuity of counsel may devise. Elsewhere in his brief he also calls attention to the decisions of the District Court in these cases, and he places much reliance thereon. These were cases decided by the District Court. In each instance they involve a state of facts not similar to the facts of the instant case, as an examination of the opinions will disclose. Furthermore, the Circuit Court of Appeals, for the Eighth Circuit, has expressly condemned the doctrine of the Rasmussen case.

In Dunlop v. Mercer, 156 Fed. Rep. 549, in a case before Sanborn and Van Devanter, Circuit Judges, and Phillips, District Judge, Justice Sanborn in rendering the opinion of the Court, among other things says:

> "The next contention of counsel for the Trustees of the Western Company is that the agreement was fraudulent and voidable against the trustees, because it permitted the conditional vendor to sell the merchandise in the regular course of busi-

> ness, but provided that the proceeds should be credited upon its notes and accounts, or held as collateral security therefor, and because it was not filed or recorded in due time in any public office; and they cite authorities from New York, Illinois, and Oregon, which sustain that position. In re Garcewich (N. Y.), 115 Fed. 87, 53 C. C. A. 510; In re Carpenter (D. C. N. Y.), 125 Fed. 831; In re Galt (D. C. Ill.), 120 Fed. 443; In re Rodgers (Ill.), 125 Fed. 169, 177, 60 C. C. A. 567; In re Rasmussen's Estate (D. C. Or.), 136 Fed. 704, 706. But the general rule and the weight of authority in this country, the established rule of property in Minnesota, and the established rule in this court are otherwise."

It is thus seen that the Circuit Court of Appeals declares that the general rule and weight of authority in this country, the established rule of property in Minnesota, and the established rule of that court are opposed to the decision of District Judge Bellinger. But in any event, in both the Rasmussen and Roellich cases, the Trustee had possession of the property. In this case it is admitted that the bank had possession of the property and the appellee overlooks this important distinction.

In his argument under this point he also calls the attention of the court to the testimony of the cashier of the bank. We invite the court's attention to this testimony too. We ask that the court read the entire testimony. It is to be found on pages 50-66, inclusive, of the Transcript of Record. It is not impeached in

any particular and it is all the testimony adduced at the hearing before the Special Master. It clearly shows that the understanding and intention of the parties was that the title to the merchandise was to be in the bank. The Trustee is bound by this testimony. He cannot assume any other or different facts. He did not call a single witness to question this testimony and he cannot question it now. It is true, he argues, that Sondheim had unlimited power to dispose of the merchandise, and that there was no restriction of any character imposed upon his utilization of the proceeds, but the record contradicts this. Under the terms of the agreement, Sondheim was required to apply one-half of the proceeds realized from the daily sales to the reduction of the indebtedness, and as a matter of convenience and to save the bank bookkeeping, this was modified so that he was required to make weekly payments of $500.00. He deposited the proceeds realized from the sales of these goods in the bank, and in the event that he did not make the weekly payments agreed upon, his checking account was to be charged, and it was charged once in the sum of $365.00 and once in the sum of $195.00, and because he failed to make the agreed payments, possession of the merchandise was taken. The undisputed, unquestioned testimony shows this to be the fact. Appellee is, therefore, mistaken when he says that Sondheim had unlimited power to dispose of the merchandise, and that there was no restriction of any character imposed upon his utilization of the proceeds.

Appellee also argues that neither the statutes of Oregon or the decisions of that State countenance any such

thing as a "trust" by which a man can do business in his own name, deal in a shifting stock of goods, use the proceeds as he sees fit, and when his creditors seek to have his assets applied to the payment of his debts, claim immunity from attack by virtue of the secret existence of an unrecorded agreement in the execution of which the debtor has then been left in uncontrolled possession and use of his assets. This is beside the point. Sondheim is not claiming immunity from attack by reason of this agreement. The bank, as a vigilant creditor, with a bona fide obligation, is asserting its claim. It is not sought to divert this property to Sondheim but it is sought to have it applied to the reduction of a bona fide claim.

In this connection, appellee also says that it is believed the court will be at least equally interested in the manner in which the transaction was actually carried out as in the language of the agreement. We have not confined ourselves simply to a discussion of the language of the agreement. We say that the language of the agreement, construed in the light of the conduct of the parties, is clear. We submit that an examination of the acts of the parties will not instantly condemn the agreement as in its nature essentially and necessarily a fraud upon the creditors, as appellee declares. During the time that Sondheim was in possession, nothing prevented his creditors from levying attachments. They were not vigilant to protect their interests. The bank was. Within three weeks after the execution of this agreement, the bank had taken possession of the property, and all through the consideration of this case it

must be remembered that Sondheim's possessions were increased by the bank, not diminished. It appears that all of this money was money used by Sondheim for different purchases of merchandise. It is admitted that $2600.00 was used to purchase the stock of merchandise in question, and the cashier of the bank testified as follows concerning the remaining sum of $2600.00:

> "At that time he owed us $2600.00 on three different notes. From time to time we advanced Sondheim money for different purchases, and at this particular time he owed us $2600.00 besides the $2600.00 advanced him on that day. (Transcript of Record, page 52.)

Speaking of such a transaction, Mr. Black in his work on bankruptcy, at page 807, says:

> "Where a bank or an individual advances money to a merchant to enable him to buy or import a stock of goods, and the merchant executes a trust receipt, by which he agrees to hold the goods in trust for the one so advancing the funds and as the latter's property, but with liberty to sell the same in the course of trade and binding him to pay over the proceeds of such sales as fast as received until the advances are repaid, the title to the goods before repayment does not vest in the merchant in such sense that they will be assets of his estate in bankruptcy, but the cestui que trust will be entitled to reclaim the goods from the trustee in bankruptcy, or the proceeds if sold."

The record shows that the bank advanced the money to enable Sondheim to make the purchase of the stock of merchandise. It shows that he executed a trust receipt. It shows that he understood and the bank understood that the title to the merchandise was to be in the bank until the indebtedness was repaid. The agreement itself, which is in evidence, recites:

> "It is understood and agreed between the parties hereto that the goods, wares and merchandise heretofore named were purchased with the money furnished by the party of the second part, and that said D. Sondheim holds title in the same as Trustee for the said party of the second part in so far as the holding of said title is necessary to protect and pay back to the party of the second part the sums of money owing by the party of the first part to the party of the second part."

The testimony of the cashier of the bank shows that payments were made on the indebtedness and that provision was made for the repayment of the entire sum owing the bank within a period of less than eleven weeks. It shows further that the agent of Mr. Sondheim in charge of the stock of merchandise, acknowledged the right of the bank to possession thereof. This was brought out by appellee on the cross-examination of Mr. Eckern. The particular questions and answers are as follows:

> "Q. While ago when I was trying to

make a statement of the facts, I made the statement that you had taken charge of the place on the 13th of November and was interrupted with the correction that someone from that place came up and surrendered the stock to you, not that you took possession; who was it surrendered that stock to you on that day; what was the reason for that correction?

A. We talked with Nudleman, the man who had charge of the store before we attempted to do this, and he said to us that we could take charge of it at any time we desired.

Q. Did he tell you why?

A. He knew that money was coming to us, that Sondheim owed us money on the stock and when we said that we thought it best to take possession ourselves he made no objection; in fact he said he knew we had a right to take it.

Q. And you sent your man over there on the 13th and took charge?

A. Yes." (Transcript of Record, pages 64-65.)

Under these circumstances the title to the merchandise did not vest in the trustee in such sense that the merchandise can be claimed as part of the bankrupt estate.

II.

Considered as a chattel mortgage, the agreement is valid under the laws of the State of Oregon.

The Special Master found that the agreement between the bank and Sondheim amounted in effect to a chattel mortgage and was void under the laws of the State of Oregon. The District Court overruled our exception to this finding. We contended then, and contend now, that the agreement does not amount in effect to a chattel mortgage. The language of the agreement considered in connection with the testimony of the cashier of the bank is clear. The title to the merchandise was to be in the bank, and if the title was in the bank the instrument clearly could not be a chattel mortgage. The testimony is clear and plain on this point. Mr. Eckern says:

> "That the stock would be considered as ours and handled for us." (Transcript of Record, page 51.)

And again:

> "Mr. Sondheim said that we would have the title but he wanted to handle the goods, to look after the managing part of it." (Transcript of Record, page 51.)

And again:

> "After we were paid $5200.00 then he would *get the title back* to the stock and we would have nothing to do with it. That was the understanding." (Transcript of Record, page 51.)

And again:

> "Our understanding was that the stock would be in our name, that we would own title to it until we were paid." (Transcript of Record, page 60.)

But even if the instrument could be held to amount in effect to a chattel mortgage it is valid under the laws of the State of Oregon. Accepting, for the sake of argument, the assumption of the appellee that the instrument is a chattel mortgage, his second assumption that it is void under the laws of the State of Oregon, is even more erroneous than his first assumption. The instrument considered as a chattel mortgage is not void under the laws of the State of Oregon. Appellee's chief objections to the instrument considered as a chattel mortgage are first, that it was not recorded, and second, that it permitted Sondheim to remain in possession of the merchandise, selling it in the usual course of business without accounting to the bank. The first objection is expressly overcome by the evidence that the agreement was entered into in good faith, for a valuable consideration and without any intent to defraud creditors, and the findings of the Special Master to the same effect. As we pointed out in the brief we first filed, at

pages 18 and 19, the failure to record a chattel mortgage raises a presumption of fraud which is overcome by evidence that the mortgage is executed in good faith and for a valuable consideration.

Subdivision 40 of Sec. 799, Lord's Oregon Laws, expressly makes the presumption from the failure to record, or from the failure to deliver possession, a disputable one, and in construing the section the Supreme Court of Oregon has construed it to mean just what it says:

In Marks vs. Miller, 21 Ore. 317, the court says:

> "Hence, a chattel mortgage under our statute, given in good faith, although not filed, is valid as against creditors and subsequent purchasers . . . . It is true in the earlier decisions the presumption of fraud from possession was held to be conclusive, but the later and better considered cases hold that the fact of possession by the mortgagor is only prima facie a badge of fraud; that it may be rebutted by explanation showing the transaction to be fair and honest and consistent with the terms of the contract; and that the presumption of fraud arising from the circumstances of such possession is not an absolute inference of law but one of fact for a jury."

In Davis vs. Bowman, 25 Ore. 189, 35 Pac. 264, the court says:

> "As to such mortgages, not recorded or filed, there is a presumption of fraud

> which, unexplained, leaves them invalid, but which when explained, removes such presumption and leaves them intact and valid."

The objection that the instrument was not recorded is also overcome for another reason—the bank took possession of the property; and while on this point it may be well to answer certain assertions of the appellee concerning this possession. The appellee in his brief intimates that the bank never had a sufficient possession of the property. This intimation is unwarranted. Paragraph III of appellee's petition contains this allegation:

> "That under which said mortgage the said bank took possession of said stock at 4 o'clock on the afternoon of Friday, November 13, 1914." (Page 12, Transcript of Record.)

The finding of the Special Master is as follows:

> "Before, however, this store could be taken into custodia legis, respondent bank, becoming apprised of the situation, entered the store, took possession and placed in charge one Eftland as agent or representative. This was upon the same day, and but a few hours before, the attempt to levy the attachment was made. Consequently, no levy could be made of the writ and this store was at no time levied upon." (Transcript of Record, page 35.)

The stipulation between the parties is as follows:

> "That an attempt was made to levy on the stock in question but that the same could not be levied because at a previous hour on the same day the agent of D. Sondheim, previously in charge of same, had surrendered the stock to the Scandinavian-American Bank." (Transcript of Record, page 48.)

The testimony of the cashier of the bank is as follows:

> "Q. State whether or not you had possession of this stock of goods at the time the attempted levy was made.
>
> A. We had." (Transcript of Record, page 55.)

And again, referring to a conversation with the agent of D. Sondheim in charge of the store, he says:

> "A. We talked with Nudleman, the man who had charge of the store before we attempted to do this, and he said to us that we could take charge of it at any time we desired.
>
> Q. Did he tell you why?
>
> A. He knew that money was coming to us, that Sondheim owed us money on the stock and when we said that we thought it best to take possession ourselves he made

no objection; in fact he said he knew we had a right to take it.

Q. And you sent your man over there on the 13th and took charge?

A. Yes." (Transcript of Record, pages 64-65.)

Appellee's petition further alleges:

"That said bank has refused to deliver possession of said stock although demand has been made upon it for the same." (Paragraph VII, Transcript, page 13.)

Also in Paragraph X:

"That the said bank is now selling the said stock at retail." (Transcript, page 13.)

This sufficiently shows that there is no basis for appellee's assertion that the possession of the bank was not open, exclusive or notorious, or that it was not taken and continued so as to give its possession these attributes. If the bank did not have the open, exclusive and notorious possession of the merchandise, why did the Special Master find that the Bank was in possession of the merchandise and that consequently a levy of the writ of attachment could not be made and that the store was at no time levied upon? If the Bank did not have possession of the merchandise why did the appellee al-

lege that it took possession of said stock Friday, November 13, 1914, at 4 o'clock p. m. and that it refused to surrender possession and that it was selling the stock at retail. If the Bank did not continue in the open, notorious and exclusive possession of the merchandise why did the appellee apply to the District Court for an order restraining the Bank from selling the merchandise at retail and why in fact did an order of the District Court issue restraining the Bank, its servants, agents and employees, no other party, from disposing of the merchandise pending the determination of the court as to its ownership? Appellee's brief is filled with just such unwarranted assertions. We can conceive of no reason why he should not be bound by his pleadings, by his stipulations and by the uncontradicted testimony.

In view of the fact that Efteland was placed in charge of the merchandise by the Bank as its agent, the following excerpt from the opinion of Mr. Chief Justice Lord in In Re Fisher, 25 Ore. 67, is very pertinent:

> "We may premise that it is not necessary that the mortgaged goods must be delivered to the mortgagee in person, but that delivery to a third party as his agent is equally effective as constituting an actual change of possession. In the case at bar, neither the mortgagor nor his clerk was left in the possession of the goods as agent for the mortgagees, but a third party, as their agent, took possession of such goods, and remained in the continued possession of the same until ousted by the sheriff under the attachment proceedings. There is a marked difference, as in-

> dicating a change in the possession of the property, between a mortgagee, or a third party as his agent, taking possession of mortgaged goods, and such mortgagee leaving the same in the possession of the mortgagor or his clerk as such agent. In the nature of things, when there has been delivery of the mortgaged goods, and an acceptance of them by a third party as such agent, his possession, so long as it continues, is actual and exclusive for the mortgagee. Nor is it necessary that there should be any removal of the goods to indicate such change of possession; for the taking of possession and assuming control over the property by such agent is an outward act, or visible sign, of an actual change of possession."

Appellee also asserts at page 23 of his brief that after the bank had become apprised of the fact that suits had been instituted by creditors and attachments issued, a few hours before the levy of attachment was made, it placed a man named Efteland in charge of the stock.

There is no testimony in the record to support this assertion. There is no evidence that the bank knew that any suits had been instituted and writs of attachment issued. As a matter of practice appellee knows that neither the sheriff or the clerk of the Circuit Court publish such information until the attachments actually have been levied. It is true that the Special Master in his report, Transcript,p. 35, says:

> "On November 13, 1914, actions were

> brought by creditors against Sondheim and writs of attachment issued against his several mercantile establishments, the one in controversy among others. Before, however, the store could be taken in the custodia of legis, the respondent bank becoming advised of the situation entered the store, took possession and placed in charge one Eftland, as agent or representative."

This language is ambiguous without a resort to the evidence. It then becomes clear that it is not intended to amount to a statement that the bank knew that suits had been instituted and attachments issued for the uncontradicted testimony discloses that the bank took possession of the merchandise because Sondheim could not be found and had not made the payments as he promised. Transcript of Record, testimony of Anthon Eckern, pp. 55, 63, 64, 65. If the bank knew that suits had been instituted and attachments issued and for that reason took possession of the merchandise appellee has not produced any witness to so testify and in the absence of any testimony to that effect his assertion is not warranted.

This answers appellee's assertions concerning the nature of the possession of the bank and the reason therefore. Returning now to the point that the possession of the bank dispensed with the necessity to record the agreement, if it be considered as a chattel mortgage, Jones in his work on chattel mortgages has this to say:

> "If a mortgagee takes possession of the mortgaged chattels before any other right

> or lien attaches, his title under the mortgage is good against everybody. If it was previously valid between the parties although it be not acknowledged and recorded or the record be ineffectual by reason of any irregularity, the subsequent delivery cures all such defects and it also cures any defect there may be through an insufficient description of the property. The delivery of possession under a mortgage before rights have been acquired by others will cure any invalidity there may be in the instrument whether arising from an insufficient description of the property and insufficient execution of the instrument, the omission to record it, or from its containing a provision which makes it void except as between the parties, as for instance an agreement that the mortgagor may retain possession and sell a stock of goods in the usual course of trade."

The statement of the author is in accord with the great weight of authority. Appellee declares, however, that the possession that will obviate the necessity for record must be an immediate one. He says:

> "The Oregon statutes in both instances precisely and explicitly declare that the only change of possession which applies is the 'immediate' change, i. e., one made promptly upon the execution and delivery of the instrument. The failure to record, therefore, was not cured by this belated taking of possession." (Appellee's Brief, page 24.)

In support of this remarkable doctrine he cites Pierce

vs. Kelly, 25 Ore. 95. This case is not authority for his contention. It was a case which turned largely upon the question of whether or not there had been a sufficient delivery of the mortgaged property to the plaintiff who was an employee of the mortgagor. Nowhere in the opinion of the court is it even intimated that the change of possession must be an immediate one to remove the presumption raised by the statute and that this is true is very apparent from the language of Mr. Chief Justice Bean in a later case construing the same statute. He says in Rule vs. Bolles, 27 Ore. 368:

> "The retention by the vendor of the possession of personal property capable of immediate delivery raises only a presumption of fraud, but this presumption continues *no longer than the property remains in the possession of the vendor;* and if, as the jury found, the possession of the horses in dispute had been delivered to, and they were under the supervision and control of, the plaintiff, at the time the defendant attached them, there was no room for the application of the rule referred to."

It is clear under the authority of this decision that the presumption of fraud raised by the statute by reason of the failure to record the agreement or to deliver immediate possession continued no longer than the property remained in the possession of Mr. Sondheim and that the moment that the bank took possession of the property the presumption ceased. This is no more than the express language of the statute itself declares. It says "creates a presumption of fraud as against the

creditors of the seller or assignor, *during his possession.*" Accordingly, the objection that the instrument was not recorded is entirely overcome, first because the instrument was executed in good faith and for a valuable consideration, and second, because the possession of the bank dispensed with the necessity of record.

Appellee's second objection is the one to which he attaches the most importance. He says that under the authority of Orton vs. Orton and like cases, the agreement is clearly void because it permitted Sondheim to remain in possession of the merchandise, selling it at retail without accounting for the proceeds. A proper consideration of this objection necessitates consideration of the testimony adduced at the hearing before the Special Master. As we have heretofore pointed out, Sondheim did not have unlimited power to dispose of the merchandise and restrictions were placed upon his utilization of the proceeds. The agreement provided for a payment of one-half the proceeds realized from the daily sales. The agreement further provided that no sale of the goods in bulk could be made without the consent of the bank. The testimony discloses that the requirement that one-half of the proceeds of the daily sales be applied to the indebtedness, was modified in order to save bookkeeping, and that in lieu thereof, Sondheim agreed to make weekly payments of $500.00, and consented, in the event that the weekly payments were not made, that his checking account should be charged therewith. The evidence shows that he deposited all the proceeds realized from daily sales in this bank. The evidence discloses that he made the first weekly payment of

$500.00, and that the second week his checking account was charged with the sum of $365.00, and that the third week his account was charged in the sum of $195.00, and possession of the merchandise taken by the bank. It is seen, therefore, that provision was made for the repayment of the entire indebtedness within a period of less than eleven weeks, and that payments were actually made, and that because the required payments were not made, that the bank took possession of the merchandise.

Now because the parties did not provide for the payment of all the proceeds realized from the daily sales, the appellee contends that the agreement is void notwithstanding that it was executed in good faith, and without any intent to defraud creditors. To support this contention he relies upon Orton vs. Orton, 7 Ore. 748, and like cases.

In each instance these early cases held the mortgage void for the reason stated by Mr. Justice Moore in Fisher vs. Kelly, 30 Ore. 1: "It is for the mortgagor's own use and benefit." Thus in Orton vs. Orton, 7 Ore. 478, the court says:

> "The evidence proves that after the execution of the first mortgage Iri Orton permitted his son M. W. Orton, the mortgagor, to sell the mortgaged goods which was a stock of merchandise and apply the proceeds to his own use."

So too in Bremer vs. Fleckstein, 9 Ore. 274, the court says: "We find the mortgagor in reality under no more restraint than if the mortgage had not been

given." Also in Aiken vs. Pascall, 19 Ore. 493, cited by the appellee, the court says, in addition to calling attention to the fact that the transaction was permeated with actual fraud, that the morgagor applied the proceeds to his own use. In none of the cases relied upon by appellee did the mortgagor pay any of the proceeds realized from the daily sales to the mortgagee to apply on the mortgage debt. Herein lies the vital distinction between the present case and the cases relied upon by appellee. In the instant case provision was made for the payment of one-half of the proceeds realized from the daily sales. In practice in order to save bookkeeping Sondheim agreed to pay a lump sum of $500.00 each week. By this provision for the payment of $500.00 each week, the agreement clearly became one for the benefit of the bank and not one for the benefit of Sondheim. Without this requirement of weekly payments, the agreement considered as a chattel mortgage, clearly would be one for the benefit of the mortgagor and the reason for holding it void against attaching creditors would be apparent. The validity or invalidity of a chattel mortgage under these decisions is to be determined in each instance by an inquiry into whether it is for the benefit of the mortgagor or for the benefit of the mortgagee. Clearly if the mortgagor retains possession of the mortgaged property selling it at retail without making any payments upon the mortgaged indebtedness, the mortgage is invalid against attaching creditors for the reason that it is for his benefit. On the other hand if the mortgagor retains possession of the mortgaged property, selling it at retail and provision

is made for weekly payments which will extinguish the indebtedness within a reasonable time the mortgage is clearly one for the benefit of the mortgagee and is valid.

This is the reasoning of the Supreme Court of Oregon in Currie vs. Bowman, 25 Ore. 364, and Sabin vs. Wilkins, 31 Ore. 450. Appellee seeks to disparage the effect of the decision in the case first mentioned by remarking, "just what aid or comfort appellant gathers from that decision is not apparent." He overlooks this very pertinent language of Mr. Chief Justice Lord:

> "It is only when the mortgage is given and received with the intent to hinder and defraud creditors that it is void and not when it is taken by the mortgagee for the honest purpose of securing a valid claim or indebtedness."

He fails to take into consideration this further observation of Mr. Chief Justice Lord in the same case:

> "A debtor has the right to secure a creditor and if he does so by giving a mortgage, it is what the law admits to be rightful, although the effect will be to hinder other creditors, and he so intends; yet if such mortgage is accepted in good faith it is not a fraudulent hindrance, because the debtor has not disposed of his property in a way to prevent its application to the satisfaction of his bona fide debts. Sabin vs. Fuel Co. (Or.), 35 Pac. 694."

Appellee also would insist that Sabin vs. Wilkins,

31 Ore. 450, is not in point but an examination of the opinion in that case rendered by Mr. Justice Wolverton, will show that it is very much in point. In reviewing the early decisions of the Supreme Court of Oregon he says:

> "It has been decided in this state that when it appears either upon the face of the mortgage or by parol evidence aliunde that the mortgagee of personal property has given the mortgagor unlimited power and authority to dispose of the property in the usual course of trade, for his own use and benefit, the mortgage is void as to attaching creditors."

It is proper to note that he says a mortgage which is for the mortgagor's own use and benefit is void, and furthermore, that the class to which it is void is attaching creditors. He then states that the creditors can only complain when the mortgage is used as a shield for the special benefit of the mortgagor and that it is the erection of a false muniment not intended to secure the mortgagee so much as to ward off and defeat just demands that works the iniquity and to avoid which the law affords a remedy.

These decisions leave no doubt as to the validity of the agreement considered as a chattel mortgage. But argues the appellee a mortgage which does not provide for the payment to the mortgagee of all the proceeds realized from daily sales is one exclusively for the benefit of the mortgagor, and therefore void. This does not follow. Each case must stand upon its own facts. The

Supreme Court of Oregon has never declared any such doctrine to be the law and as said by the Supreme Court of the United States in Etheridge vs. Sperry, "the question is not one of law so much as it is one of fact and good faith," and in this case the Special Master expressly found that the bank entered into the contract with Sondheim in good faith and with no actual intent upon its part to hinder, delay or defraud creditors. In the light of the decisions of the Supreme Court of Oregon, under the admitted facts of the instant case, it is clear that considered as a chattel mortgage the agreement was one for the benefit of the bank and valid.

In this connection the decision of the Supreme Court of Alabama, in Adkins vs. Bynum, 109 Ala. 281, emphasizes a distinction that should be given consideration. The court in that case said that while constructive fraud is imputed to a transaction by which a mortgagor retains possession of mortgaged property, selling it at retail for his own use and benefit, that constructive fraud cannot be imputed to a transaction where the mortgagee has furnished the property to the mortgagor, and the mortgagor is holding the property as security to repay the mortgagee, even though he sells it at retail for his own use and benefit. In its opinion the court says its attention has not been called to any decision pointing out this distinction, but, continues the court, it is one that should be made. The court sums the matter up in these words:

> "So that in any view, the creditor loses nothing and cannot be hurt by such a

transaction, and he may well be substantially benefited."

(c) *Possession of mortgaged property by a mortgagor under an unrecorded chattel mortgage before the lien of any creditor attaches, makes such a mortgage good against every one.*

The Scandinavian-American Bank had possession of the merchandise in controversy before the lien of any creditor attached, and before the proceedings in involuntary bankruptcy were instituted. If, for any reason, the agreement considered as a chattel mortgage could be said to be invalid against creditors this possession of the bank cured all defects and made it valid and binding. We refer the court again to the authorities which we cited in the brief which we first filed which are found under this point on pages 20, 21 and 22.

The appellee calls the attention of the court to the decision of the District Court of Oregon in Schaupp vs. Miller, 206 Fed. Rep. 575, as announcing a contrary doctrine. It will be observed in that case that the bankrupt was permitted by the mortgagee to continue in possession of the goods and sell them at retail in the usual course of business without paying any of the proceeds on the mortgage indebtedness. It will further be observed that Mr. Justice Bean says mortgages of that character are void in Oregon for the reason stated by Mr. Justice Moore in Fisher vs. Kelly, 30 Ore. 1, "It is for the mortgagor's own use and benefit," and also that there is no authoritative ruling by the Supreme Court of Oregon on the effect of possession. It is true

that he holds that possession does not validate the mortgage, but the question has never been passed upon by this court and in the absence of any decision to the contrary by the Supreme Court of the State of Oregon, we submit that the better rule, both upon reason and authority, is that possession before the lien of any creditor attaches, cures any invalidity.

Etheridge vs. Sperry, 139 U. S. 277.

Johansen Bros. Shoe Co. vs. Alles, 197 Fed. 274.

In re Marengo County Mercantile Co., 199 Fed. 480-481.

In re Harnden, 200 Fed. 177-178.

Garner vs. Wright, Ark. 6 L. R. A. 715.

Noyes et al. vs. A. E. Ross (Mont.), 47 L. R. A. 400.

Read et al. vs. Wilson, 22 Ill. 380.

First National Bank of Fergus Falls vs. Michael 24 Minn. 436.

Cameron vs. Marvin, 26 Kan. 612.

Francisco et al. vs. Ryan, 34 Ohio St. 307.

In re First National Bank of Canton, Ohio, C. C. A. 6th Circuit, 135 Fed. 62.

Thompson vs. Fairbanks, 196 U. S. 516.

Humphrey vs. Tatman, 198 U. S. 94.

Hauselt vs. Harrison, 105 U. S. 405.

The decision of the Circuit Court of Appeals for the Eighth Circuit, in Johansen Bros. Shoe Co. vs. Alles, 197 Fed. 274, will be found squarely in point. The statutes of the State of Missouri with reference to the

validity of chattel mortgages are similar to the statutes of the State of Oregon. The case is a recent one.

Likewise in Cameron vs. Martin, 26 Kansas 612, the Supreme Court of Kansas goes carefully into the question of the effect of possession by a mortgagee. This was a case where the plaintiffs claimed the property by virtue of four chattel mortgages which were never recorded, and they did not take possession of the property until long after the mortgages were executed. Nine days after such possession was taken, the defendants issued a writ of attachment against the mortgagor and levied it upon the property. The court held that the mortgages were valid from the time the mortgagees acquired possession of the property covered by the mortgages.

Mr. Justice Valentine, in delivering the opinion of the court, observed:

> "We now come to the question, would the mortgage become valid when the plaintiffs took possession of the property under them? We think we must answer this question in the affirmative. (Dayton vs. Savings Bank, 23 Kan. 421; Savings Bank vs. Sargent, 20 Kan. 576; Nash vs. Norment, 5 Mo. App. 545; Eastman vs. Water Power Co., 24 Minn. 437; Reed vs. Wilson, 22 Ill. 377; Frank vs. Minor, 50 Ill. 444; Chipron vs. Feikert, 68 Ill. 284; McTaggart vs. Rose, 14 Ind. 230; Brown vs. Platt, 8 Bosw. (N. Y.), 324; Brown vs. Webb, 20 O. 389; Chapman vs. Weimer, 4 Ohio St. 481; Field vs. Baker, 12 Blatch (U. S. 438.)"

After quoting section 178, Jones on Chattel Mortgages, to the effect that possession cures any invalidity there may be in the instrument, or from its containing a provision which makes it void as between the parties, the opinion continues:

> "This statement of the law is undoubtedly in accordance with the great weight of authority . . . Of course, a chattel mortgage for property not delivered is void as against all creditors who have no notice of the mortgage, but they have no right to, or interest in any specific property until they have obtained this right or interest by some legal process. They have no more right to the property than the mortgagee has, whose mortgage is void. They all have an equal right to the property, that is, they all have a right to procure a lien upon it, or an interest in it by virtue of legal process or chattel mortgage or purchase; and the one who first acts will obtain the prior right in and to the property. If one of the creditors already has a chattel mortgage upon the property he may file his mortgage or procure possession of the property, and if he has done this with the consent of the mortgagor, he has certainly obtained the prior right to the property."

In Wilson vs. Leslie, 20 Ohio, 161, under a statute which declared that every mortgage upon chattels which shall not be accompanied by *immediate* delivery and be followed by an actual and continued change of possession, shall be absolutely void as against creditors, subsequent purchasers and mortgagees in good faith, unless

the mortgage shall be forthwith deposited as directed in the succeeding section of the act, the Supreme Court of Ohio said:

> "A fair construction of this statute will not make the instrument inoperative as between the parties although it be not forthwith deposited with the recorder . . . The mere fact that the mortgagee omitted for several days or weeks to deposit his mortgage with the clerk of the township or recorder of the county as the case might require, would by no means render his security void. It would not be void against that class of creditors who were equally remiss with the mortgagee and took no steps to fasten upon the property for the payment of their debts."

In Forrester vs. Kearney National Bank, the Supreme Court of Nebraska declares that possession by a mortgagee before the right or lien of any third party attaches, makes the mortgage good against everybody.

In Francisco et al. vs. Ryan, the Supreme Court of Ohio had under consideration a mortgage which permitted a mortgagor to remain in possession of a stock of merchandise with a power of sale. The court held that such a mortgage was ineffectual to create a lien as against creditors of the mortgagor who asserted their rights against the property while it remained under his control, but that it was valid as between the parties, and when the mortgagee took possession, the property was not longer subject to legal process issued against the mortgagor or liability for his debts, except to the extent

of any surplus that might remain after the satisfaction of the mortgage debt and proper charges for enforcing the same.

It is clearly apparent under the authority of this case and like cases that even if this court should be of the opinion that the agreement between the Scandinavian-American Bank and D. Sondheim constituted a chattel mortgage and was void because he did not pay all the proceeds to the bank, that the fact that the bank secured possession before the lien of any creditor attached, entitled it to hold the property.

The case, however, which we deem decisive of this question is Hauselt vs. Harrison, 105 U. S. 405. This was a case where the defendant, Harrison, entered into an agreement with one Edward Bayer by which he advanced certain moneys to Bayer for the purchase of veal and kip skins, under a provision that all the skins should be considered a security for the advances. The agreement was not acknowledged, nor was it recorded, and plaintiff as assignee in bankruptcy of Bayer, sought to recover skins which the defendant had taken possession of. The Supreme Court says:

> "It was decided in Gregory vs. Morrison, 96 U. S. 619, that the legal effect of such a contract is to create a charge upon the property, not in the nature of a pledge, but of a mortgage. Such a lien is good between the parties without a change of possession even though void as against subsequent purchasers in good faith without notice, and creditors levying executions or attachments.

And if followed by a delivery of possession before the rights of third persons have intervened, it is good absolutely."

The court then proceeds to say that the equitable lien created by the arrangement between the defendant and Bayer was one capable of enforcement, and reversed the decision of the lower court and confirmed the defendant in his possession of the property.

The Scandinavian-American Bank enabled Sondheim to make the purchase of this merchandise. It secured possession before the rights of third persons intervened. The trustee is not a subsequent purchaser in good faith, without notice, and no creditors effected a levy of executions or attachments prior to the possession of the bank. Under the authority of this decision alone, the decree of the District Court should be reversed.

(*d*) *Even without a change of possession, an unrecorded mortgage given in good faith is good against every one but subsequent purchasers and mortgagees in good faith and for a valuable consideration of the same personal property.*

Appellee has failed to make any sufficient answer to this contention. Section 4707 Lord's Oregon Laws provides in substance that every chattel mortgage which shall not be accompanied by immediate change of possession, or which shall not be recorded, shall be void as against subsequent purchasers and mortgagees in good faith and for a valuable consideration. The statute does not say that such a mortgage shall be void against all

creditors. Its operation is limited to subsequent purchasers and mortgagees in good faith and for a valuable consideration.

The trustee is within neither of these classes. He is neither a subsequent purchaser nor a mortgagee. He calls the court's attention to an excerpt from Section 799, Lord's Oregon Laws. He fails to consider that the presumption of fraud raised by that section is a disputable one and that it is removed by evidence that the agreement is entered into in good faith and for a valuable consideration and without intent to defraud creditors. He fails also to consider that this presumption continues no longer than the property remains in the possession of the assignor or mortgagor and that as soon as the possession of the assignor or mortgagor ceases, the presumption ceases. The trustee stands in the shoes of the creditors. They fastened no lien upon this property. They were not in a position to question this agreement. They could not set it aside. The trustee cannot do what they could not do.

III.

The trustee is without authority to maintain this proceeding.

Appellee's argument under this point is very interesting. He contends that under the laws of the State of Oregon a general creditor could attack the transaction between Sondheim and the bank, and cites in support of this contention Jacobs vs. Ervin, 9th Ore. 52. The de-

cision in that case is not applicable to the facts of the instant case for two important reasons. First, the property covered by the assignment in that case at all times remained in the possession of the assignor and he voluntarily executed an assignment to the assignee, and second, the actual possession of the property passed directly from the assignor to the assignee. Appellee is clearly mistaken when he claims that the case is authority for the proposition that a general creditor, or his assignee who stands in the shoes of the general creditor could, in the absence of any lien, proceed against a third party to recover property in that party's possession.

Discussing the case upon which appellee relies as supporting his contention, Mr. Justice Deady in Hahn vs. Salmon, 20 Fed. 807, says:

> "In Jacobs vs. Ervin, 9 Ore. 57, the Supreme Court of the State held that 'when a mere lien or incumbrance, fraudulent and void as to creditors, but valid as between the parties, has been created by the assignor upon property remaining in his possession, and the title to which passes to and vests in the assignee for the benefit of creditors,' the assignee, as the representative of such creditors, may resist the assertion or enforcement of such fraudulent lien or incumbrance. But neither the opinion nor the case goes further than this, and in the former it is plainly implied that this power of the assignee only extends to the defense or protection of property of which he has both the possession and title, from the effect of a fraudulent lien or incumbrance."

He says further:

> "An insolvent debtor, who has made a fraudulent transfer of his property for the purpose of defrauding his creditors, cannot reclaim it; nor can he confer a right in this respect upon another which he does not himself possess."

It seems that this would sufficiently answer appellee's claim that a general creditor could impeach the transaction between Sondheim and the bank. That Mr. Justice Deady is correct in his interpretation of this decision rather than appellee is apparent from subsequent decisions of the Supreme Court of Oregon.

In Gammons, assignee, vs. Holman et al., 11 Ore. 284, 3 Pac. 676, the rights of an assignee were before the court. One Klingel was indebted to the defendants. He entered into a parol agreement with them by which they were to make certain advances to enable him to secure certain goods which were consigned to him, and which they were to hold until he repaid all the indebtedness owing them. The defendants received possession of the goods but in the meantime Klingel had made an assignment for the benefit of all his creditors covering the goods in question. The court held that the assignee had no greater right to the goods than Klingel, and since he could not claim the goods, the assignee could not, and this in spite of the fact that the assignment was made before the defendants secured possession of the goods.

Justice Bean in Helms vs. Gilroy, 20 Ore. 517, 26

Pac. 851, speaking of the rights of an assignee under the general assignment law, says:

> "The defendant Rogers, who alone is contesting plaintiffs' claim, is the assignee of the defendant Gilroy, plaintiffs' mortgagor, under the general assignment law of this state. As such assignee, he succeeds only to the rights of his assignor, and is affected by all the equities existing as against him. He takes the property subject to all existing valid liens and charges. He acquires no better title than his assignor, and, in this suit, can make no defense to the mortgage that his assignor could not make."

Justice Moore in Fisher vs. Kelly, 30 Oregon 1, 46 Pac. 148, discussing a chattel mortgage which was held void because it was for the mortgagor's own use and benefit, says:

> "The general creditor is in no position to raise the question that the mortgage is void as to him until he has seized the property covered by the chattel mortgage, or secured some lien thereon."

The case last mentioned, Fisher vs. Kelly, 30 Ore. 1, is cited by appellee in his brief and is a case which involved the validity of a mortgage with a so-called power of sale. Its language is clear and plain. The general creditor is in no position to raise the question that the mortgage is void as to him until he has seized

the property covered by the chattel mortgage or secured some lien thereon, and this the creditors of the bankrupt failed to do. The trustee stands in the shoes of these creditors. He can assert no rights they did not assert. They secured no lien upon this property and they are, therefore, not in a position to raise the question that the agreement is void, and he cannot raise a question they did not raise.

Mr. Justice Ross in the Flatland case passed squarely upon this point. In that case, counsel for the petitioner contended that while the mortgage was good between the parties, it was not good against the trustee, and that under the amendment of 1910, the trustee did not stand in the shoes of the bankrupt but had all the rights of a creditor possessing a levy upon the property in controversy, and that if the lien of the mortgage would not, for any reason, be valid against a levying creditor, it would not be valid against the trustee. Answering this contention, Mr. Justice Ross, speaking for the court, said:

> "A conclusive answer to the suggestion here made is that there is nothing in the record showing that any of the creditors of the bankrupt other than the respondent held a lien of any character."

Precisely the same situation exists in this case. None of the creditors other than this appellant held a lien of any character. The appellee is clearly without authority to maintain this proceeding.

Notwithstanding the decision of this court in the

Flatland case, appellee asserts that he has authority to maintain this proceeding under section 70a5. This contention proceeds upon the assumption that a general creditor could impeach the transaction between Sondheim and the bank. We have shown that under the direct and positive language of the Supreme Court of Oregon, this assumption of appellee's is unwarranted.

> "A general creditor is in no position to raise the question that the mortgage is void as to him until he has seized the property covered by the chattel mortgage or secured some lien thereon." Fisher vs. Kelly, 30 Ore. 1.

Discussing Section 70a5, Mr. Collier in his very valuable work on bankruptcy, pp. 996-997, says:

> "That it is well settled that the trustee in bankruptcy takes not as an innocent purchaser, but subject to all valid claims, liens and equities, and that he has no better title than the bankrupt had, and is affected with every equity which would affect the bankrupt himself if he were asserting the same rights or interest."

The decree of the District Court should be reversed.

Respectfully submitted,

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Attorney for Petitioner and Appellant.